

# **REPORT OF THE AUDITOR-GENERAL TO THE FREE STATE LEGISLATURE AND THE COUNCIL ON FINANCIAL STATEMENTS OF THE MANTSOPA LOCAL MUNICIPALITY**

## **REPORT ON THE FINANCIAL STATEMENTS**

### **Introduction**

1. I have audited the accompanying financial statements of the Mantsopa Local Municipality, which comprise the statement of financial position as at 30 June 2011, and the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information, as set out on pages ... to ....

### **Accounting officer's responsibility for the financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standard of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and for such internal control as management determines necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor-General's responsibility**

3. I conducted my audit in accordance with International Standards on Auditing and General Notice 1111 of 2010 issued in *Government Gazette 33872 of 15 December 2010*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

## **Basis for qualified opinion**

### **Property plant and equipment**

6. Included in work in progress were additions amounting to R 16 070 824 that were disclosed in note 7.3 to the financial statements. I could not verify the accuracy and completeness of this amount, as the additions were not included in the asset register as per the requirement of GRAP 17 for work in progress. Consequently, I could not verify the accuracy and completeness of the amount that should have been disclosed in the financial statements. The municipality's records did not permit the application of alternative audit procedure regarding the accuracy and completeness of work in progress.
7. The depreciation rates used to calculate the depreciation amount as disclosed in the statement of financial performance and note 7.1 to the financial statements were considered to be excessive and could not be justified when compared to similar municipalities. Consequently depreciation is understated and property plant and equipment is overstated by an unknown amount. The municipality's records did not permit the application of alternative audit procedures regarding the accuracy of depreciation.
8. The change in accounting policy relating to property, plant and equipment to the value of R 139 080 316 as disclosed in the statement of changes in net assets and note 23 of the financial statement in terms of the requirement of GRAP 3 is not accurate. Had the change in accounting policy been accurately disclosed the change in accounting policy should have been R 115 906 056 therefore the accumulated surplus is overstated by R 23 174 258 and the property plant and equipment overstated by R 23 174 258.

### **Accounts payable**

9. I was unable to verify the completeness and valuation of accounts payable, stated at R16 511 966 in the financial statements. The municipality imposed a limitation on the scope of my work, as I could not be provided with sufficient appropriate evidence to verify the valuation and completeness of accounts payable. The municipality's records did not permit the application of alternative audit procedures regarding the valuation and completeness of accounts payable.

### **Accounts receivable**

10. I was unable to verify the existence and valuation of accounts receivable stated at R 3 783 918 in the financial statements. The existence of debtor's could not be verified, as debtors did not pay their accounts subsequent to year- end. Evidence could not be provided to indicate the existence of these debtors. The municipality imposed a limitation on the scope of my work, as I could not verify whether debtors would be recovered. The municipality's records did not permit the application of alternative audit procedures regarding the existence of accounts receivable.
11. Included in accounts receivable were debtors with a credit balance of R 2 608 345 in the financial statements. The municipality imposed a limitation on the scope of my work, as I could not be provided with sufficient appropriate evidence to verify the valuation, existence and completeness of the debtors with credit balances. The municipality's records did not permit the application of alternative audit procedures regarding valuation, existence and completeness.

**Investment property**

12. I was unable to verify the completeness and valuation of investment property, stated at R1 446 000 in the statement of financial position and note 7.2 of the financial statements, as well as the completeness of investment income as disclosed in the statement of financial performance stated at R869 315. The municipality imposed a limitation on the scope of my work, as the investment properties register and the financial statements did not include all the investment property owned by the municipality. The municipality's records did not permit the application of alternative audit procedures regarding the valuation and completeness of investment property.

**Consumer deposit**

13. I was unable to verify the completeness and valuation of the consumer deposit stated at R 1 062 312 in the financial statements. The municipality imposed a limitation on the scope of my work, as I could not be provided with sufficient appropriate evidence to verify the valuation and completeness of the consumer deposit. The municipality's records did not permit the application of alternative audit procedures regarding valuation and completeness.

**Qualified opinion**

14. In my opinion, except for the effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Mantsopa Local Municipality as at 30 June 2011, and its financial performance and cash flows for the year then ended, in accordance with SA Standards of GRAP and the requirements of MFMA.

**Emphasis of matters**

I draw attention to the matters below. My opinion is not modified in respect of these matters:

**Restatement of corresponding figures**

15. As disclosed in note 38 to the financial statements, the corresponding figures for 30 June 2010 have been restated as a result of an error discovered during the year ended 30 June 2011 in the financial statements of the municipality.

**Material Losses**

16. As disclosed in note 43 to the financial statements, material losses of R 10 314 183 were incurred as a result of a write-off of electricity losses that were purchased but were not sold. Water losses could not be determined, as bulk meters did not exist for waterworks and bore holes in towns.

**Unauthorised Expenditure**

17. As disclosed in note 42 to the financial statements, unauthorised expenditure of R 41 791 702 was incurred due to the overspending of the budget under the environmental health vote to the amount of R 527 674, the sanitation vote to the amount of R 12 123 176, the refuse vote to the amount of R 9 394 847, the water vote to the amount of R 18 657 982, the fire brigade vote to the amount of R 91 229, the properties vote to the amount of R 193 015, the parks vote to the amount of R 627 950 and the municipal manager votes to the amount of R 175 829.

### **Irregular expenditure**

18. As disclosed in note 41 to the financial statements, irregular expenditure of R 6 275 403 was incurred due to non-compliance with the supply chain management (SCM) policy and procedures as well as deviations from procurement processes.

### **Fruitless and wasteful**

19. As disclosed in note 40 to the financial statements, fruitless and wasteful expenditure of R 117 754 was incurred due to creditors not being paid within 30 days and VAT 201 forms being submitted after the closing date.

### **Additional matters**

I draw attention to the matters below. My opinion is not modified in respect of these matters:

### **Unaudited supplementary schedules**

20. The supplementary information set out on pages xx to xx does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion thereon.

### **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

21. In accordance with the PAA and in terms of *General Notice 1111 of 2010*, issued in *Government Gazette 33872 of 15 December 2010*, I include below my findings on the annual performance report as set out on pages ... to ... and material non-compliance with laws and regulations applicable to the municipality.

### **Predetermined objectives**

#### **Presentation of information**

22. The reported performance against predetermined objectives was deficient in respect of the following criterion:
- Performance against predetermined objectives was not reported using the National Treasury guidelines.
- The following audit findings relate to the above criteria:
- No measures taken to improve performance were provided in the performance report, as required in terms of section 46(1) (c) of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA). In total, 100% of the reported targets where improvement was required were not explained.

#### **Usefulness of information**

23. The reported performance information was deficient in respect of the following criteria:
- Consistency: The reported objectives, indicators and targets were not consistent with the approved integrated development plan.
  - Measurability: The targets were not time bound.

The following audit findings relate to the above criteria:

**24. Planned indicators included in the integrated development plan not consistent with the service delivery and budget implementation plan.**

In total, at least 51% of the planned indicators and targets specified in the service delivery and budget implementation plan for the year under review were not included in the integrated development plan submitted for audit purposes.

**25. Planned and reported targets not time bound**

For the selected objectives, 51% or more of the planned and reported targets were not time-bound in specifying the time period or deadline for delivery

**Reliability of information**

26. The reported performance information was deficient in respect of the following criteria:

- Accuracy: The amounts, numbers and other data relating to reported actual performance had not been recorded and reported appropriately.
- Completeness: All actual results and events that should have been recorded had not been included in the reported performance information.

The following audit findings relate to the above criteria:

**27. Reported performance against indicators and targets not valid and accurate when compared to source information**

For the selected objectives, 21% of the reported indicators were not valid and accurate based on the source information or evidence provided.

**28. The completeness of reported performance against indicators could not be confirmed as inadequate supporting source information was provided**

For the selected objectives the completeness of 21% of the reported indicators could not be established, as sufficient appropriate audit evidence and relevant source documentation could not be provided.

**Compliance with laws and regulations**

**Budgets**

29. The municipality incurred expenditure that had not been budgeted for and expenditure in excess of the limits of the amounts provided for in the votes in the approved budget, in contravention of section 15 of the MFMA.

30. Unforeseeable and unavoidable expenditure not provided for in the annual budget was incurred but was then not appropriated in an adjustment budget, as required by section 29(2)(d) of the MFMA.

**Annual financial statements, performance report and annual report**

31. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements in (capital assets/ current assets/ liabilities/ revenue/ expenditure/ and disclosure items) identified by the auditors were subsequently corrected, but the uncorrected material misstatements resulted in the financial statements receiving a qualified audit opinion.

### **Procurement and contract management**

- 32. Awards were made to providers who were persons in the service of the municipality or whose directors were persons in the service of the municipality, in contravention of SCM Regulations 44. Furthermore, the providers failed to declare that they were in the service of the municipality, as required by SCM Regulation 13(c).
- 33. Awards were made to providers who were persons in the service of other state institutions in contravention of the requirements of SCM Regulations 44. Furthermore, the providers failed to declare that they were in the service of the state, as required by SCM Regulation 13(c).
- 34. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by SCM Regulation 46(2) (e) and the codes of conduct for councillors and staff members issued in terms of the MSA.

### **Expenditure management**

- 35. Money owing by the municipality was not always paid within 30 days of receiving an invoice or statement, as required by section 65(2)(e) of the MFMA.
- 36. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained a management, accounting and information system that recognised expenditure when it was incurred as well as accounted for creditors of the municipality and payments made by the municipality, as required by section 65(2)(b) of the MFMA.
- 37. The accounting officer did not take reasonable steps to prevent unauthorised, irregular as well as fruitless and wasteful expenditure, as required by section 62(1) (d) of the MFMA.

### **INTERNAL CONTROL**

- 38. In accordance with the PAA and in terms of *General notice 1111 of 2010*, issued in *Government Gazette 33872 of 15 December 2010*, I considered internal control relevant to my audit, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters reported below are limited to the significant deficiencies that resulted in the basis for the qualified opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

### **Leadership**

- 39. The accounting officer did not take decisive action in response to the risk of non-compliance with the SCM policy and SCM Regulations, by implementing controls to prevent the occurrence of irregular as well as, fruitless and wasteful expenditure.
- 40. The accounting authority failed to exercise oversight responsibility regarding financial and performance reporting, compliance as well as related internal controls.

### **Financial and performance management**

- 41. Non-compliance with laws and regulations could have been prevented had compliance been properly reviewed and monitored.

42. Management did not implement proper record keeping in a timely manner to ensure that complete, relevant and accurate information was accessible and available to support financial and performance reporting. This resulted in a qualification on property, plant and equipment, investment property, accounts receivable, as well as accounts payable.

Bloemfontein

30 November 2011



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*